

Wilmington Trust Center, 1100 North Market Street, Suite 1001, Wilmington, DE 19801  
Tel: (302) 777-5860 ■ Fax: (302) 777-5863 ■ [www.WolfBlock.com](http://www.WolfBlock.com)

Thomas P. McGonigle  
Direct Dial: (302) 777-6374  
Direct Fax: (302) 778-7834  
E-mail: [tmcgonigle@wolfblock.com](mailto:tmcgonigle@wolfblock.com)

September 13, 2007

**VIA E-MAIL**  
**OVERNIGHT MAIL TO FOLLOW**

The Honorable Arnetta McRae  
Commission Chair  
Delaware Public Service Commission  
861 Silver Lake Boulevard  
Cannon Building Suite 100  
Dover, Delaware 19904

The Honorable Jennifer Wagner Davis  
Director  
Office of Management and Budget  
Haslet Armory  
122 William Penn Street  
3rd Floor, Suite 301  
Dover, Delaware 19901

The Honorable Russell T. Larson  
Controller General  
Office of the Controller General  
Legislative Hall  
411 Legislative Avenue  
Dover, Delaware 19901

The Honorable John A. Hughes  
Secretary  
Department of Natural Resources and  
Environmental Control  
89 Kings Highway  
Dover, Delaware 19901

Dear Chairwoman McRae, Director Davis, Controller General Larson and Secretary Hughes:

On May 22, 2007, the Delaware Public Service Commission (the "PSC"), the Office of Management and Budget ("OMB"), the Office of the Controller General ("CG") and the Department of Natural Resources and Environmental Control ("DNREC") (collectively referred to as the "State Agencies"), directed Delmarva Power & Light Company ("Delmarva") to negotiate with Bluewater Wind Delaware LLC ("Bluewater") for the construction of a wind park off the coast of Delaware. With this letter, Bluewater is pleased to notify the State Agencies that key commercial terms (the "Term Sheet") have been finalized for a proposed 450 MW wind energy facility to be constructed and operated off the coast of Delaware.

The Term Sheet, which Delmarva will submit, is the product of several months of extensive and intense negotiations between Bluewater and Delmarva, as the parties sought to resolve the many complex and novel issues presented by a transaction of this type. With the Term Sheet finalized, Bluewater and Delmarva now begin incorporating these provisions into

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the power purchase agreement (the "PPA"), which, if approved, will serve as the economic foundation for what likely will be the first offshore wind energy facility in the United States and one of the largest offshore wind energy facilities in the world. More importantly, this facility will provide the citizens of Delaware with clean energy at stable prices and will firmly establish Delaware at the forefront of the rapidly growing renewable energy industry.

We understand the State Agencies will now begin a formal evaluation of this Term Sheet. To that end, we provide this letter to: (1) highlight, explain and provide context to the agreed upon terms; (2) explain the price and price stability implications of this project; (3) make the case for an open and transparent evaluation process; and (4) discuss the remaining outstanding issues that have not been resolved.

### **PROJECT HIGHLIGHTS**

This project offers great value to Delmarva's ratepayers and the State of Delaware, providing a significant source of clean energy at stable prices - all with minimal environmental impact. With this Term Sheet, Bluewater commits to the following:

- Providing up to 300 MW of energy each hour, a level of energy sufficient to power 100,000 Delaware homes with clean renewable energy year round. In addition, this project will provide stable-priced energy that will help limit future price spikes.
- A partnership with Delmarva and the State of Delaware over the next 25 years to help control its energy future, while creating hundreds of good paying, union jobs for Delaware. Without this project, Delaware will remain overly dependent on out-of-state power for its electricity needs. This project will be a Delaware resource, regulated by the State of Delaware for the benefit of the people of Delaware. As such, this represents a critical step in Delaware's effort to gain a significant measure of control over its energy future.
- A firm timeline for constructing the project, with the first clean energy generation being produced as early June 1, 2014, but no later than the Spring of 2015. As proof of Bluewater's commitment to Delaware and this project, this timeline commitment is backed by the initial posting of millions of dollars of development security, combined with an obligation to pay penalties up to \$68 million if specified milestone dates are not achieved.

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- Providing valuable and sought after Renewable Energy Credits that Delmarva is obliged to obtain under Delaware law.
- Using state-of-the art wind turbine technology to optimize project performance and efficiency, at an expected total construction cost in excess of \$1.5 billion. This will ensure that Delaware's wind park will be on the cutting edge on the day it goes into service.
- A site location, approximately 11.5 miles off the coast of Delaware, which will maximize the quality of the project's wind resource, while minimizing environmental and visual impacts. Although we believe the project will have very positive aesthetics, at this distance from shore, the project will be barely visible to the unaided eye.
- An agreement to pay all transmission upgrades (expected to cost in excess of \$50 million), both inside and outside the Delmarva zone, as necessary to get the project's renewable energy efficiently to market.
- Full compliance, as the project moves forward, with state and federal environmental requirements. For example, with the execution of the PPA, Bluewater will begin a process whereby millions of dollars will be spent on avian, fish and other studies to ensure that environmental impacts are minimized.

### **PRICE AND PRICE STABILITY**

A critical factor in the evaluation of this project is, and should be, the ultimate cost that will have to be paid by Delmarva's ratepayers for the project's clean renewable energy over the 25 year term of the contract. With this Term Sheet, we highlight the following:

- As discussed below, Delmarva has not disclosed the assumptions and criteria it uses to estimate the actual price impact on the wind project for its ratepayers. However, Delmarva's summer rates for the first 500 kWh of energy on an average electric bill equal 10.68 cents per kWh. Delmarva's winter rates for the first 500 kWh of energy on an average electric bill equal 11.62 cents per kWh.<sup>1</sup> Bluewater's rate bid to Delmarva is

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<sup>1</sup> Again, without access to Delmarva's pricing methodology, it is not possible to determine for comparison purposes the components of this rate.

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10.59 cents per kWh. When Delmarva's capacity payments to Bluewater are factored in, the combined capacity supply energy cost to Delmarva is 10.596 cents per kWh.

- Price stability is a critical component of this Term Sheet, as the price will be guaranteed over the 25 year term of the contract -- regardless of what happens to oil prices, coal prices or natural gas prices. Indeed, this pricing structure reduces the possibility that Delaware ratepayers will again be faced with the type of 59% overnight increase due to its reliance on traditional fossil fuel production.<sup>2</sup>
- Most meteorological and environmental experts in the field believe that, due to concerns about sea level rise, climate change and energy security, the United States will inevitably move to impose carbon caps and/or a carbon tax. This will likely lead to marked increases in the price of fossil fuel-generated power -- increases that will directly pass on to Delaware ratepayers. Of course, such changes in the market will have no impact on the cost of power provided by the Bluewater project (the wind will always be free), thus providing Delaware with an important hedge against this very likely scenario.
- Oil and gas resources are concentrated in regions of the world that are politically unstable and often hostile to the interests of the United States. This reality inevitably leads to price instability and, ultimately, the risk of sudden and dramatic price increases, as already experienced by Delaware ratepayers. The impact of such geopolitical factors on the cost of power provided by the Bluewater project is zero.

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<sup>2</sup> Given the lead time between these negotiations and the possible purchase of raw materials to build the wind park, Bluewater's pricing proposal contemplates the possibility of price adjustments to reflect possible changes in raw material prices between the date of signature of the PPA and the commencement of construction.

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### TRANSPARENT EVALUATION PROCESS NECESSARY

Although Bluewater acknowledges and very much appreciates that Delmarva worked diligently during these negotiations, we fear Delmarva may oppose approval of this Term Sheet. To that end, Delmarva may argue that this project is too expensive for ratepayers, citing its own evaluation to support this claim.

Importantly, any proper evaluation of price must include a careful review of the assumptions that go into the evaluation. Throughout these negotiations, Bluewater has requested that Delmarva disclose their evaluation criteria and assumptions, so that Bluewater, the State Agencies and the public-at-large, can properly review this critical issue. To date, Delmarva has not released this information.

By way of example in terms of the importance of transparency in this process, there is the critical issue of penalties that PJM may impose related to Bluewater and the back-up provider under certain circumstances. Delmarva has indicated that this issue cannot be remedied and therefore the penalties will be incurred and must be included in its evaluation of the overall price. However, Bluewater's experts have consulted extensively with PJM and others to conclude that the penalties can largely be mitigated. Indeed, Bluewater and NRG have discussed this issue and both companies believe the issue can be resolved without the imposition of significant penalties.<sup>3</sup> Without knowing Delmarva's evaluation criteria, we will not know what Delmarva attributes to this issue in terms of price or how it may, improperly in our view, inflate Delmarva's projected price to its ratepayers.

Accordingly, Bluewater respectfully requests the State Agencies request that Delmarva fully disclose all of its evaluation criteria, so that the evaluation process is transparent and thus can be conducted with the full benefit of public review and input. In closing, the State Agencies have properly required to date that this process be transparent and open, with the

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<sup>3</sup> While Bluewater attempted to have similar dialog with Conectiv on this and other issues related to the proper coordination between the wind park and the back-up facility, Conectiv declined to execute a confidentiality agreement related to any such discussions and no such dialog was possible. In contrast, Delmarva, NRG and Bluewater all executed confidentiality agreements, thereby allowing an important free and open discussions about the logistics and coordination between generators.

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public responding with unprecedented attention to this critical issue. At this critical stage of the process, we think it important that Delmarva's evaluation criteria be disclosed.

### OUTSTANDING ISSUES

As discussed above and as provided in great detail in the Term Sheet, Bluewater and Delmarva have reached agreement on almost all of the key commercial terms for this very complex transaction. While there remain three outstanding issues that need resolution, they are rather arcane and can likely be resolved with counsel and guidance from the State Agencies.

The first issue deals with the consequence of delay that is caused by litigation initiated by Delmarva and/or Conectiv. Bluewater is concerned with contractual provisions that allow Delmarva termination rights and delay damages resulting from such litigation caused delay. The reason being, upon execution of the PPA, Bluewater will begin spending millions of dollars and has thus sought assurances that if the State Agencies approve the PPA, Delmarva and Conectiv will halt litigation efforts to kill this project. Delmarva has taken the position that it must retain its appeal rights (and it therefore would not discontinue its appeal of the State Agencies prior order authorizing these negotiations) and that it does not control its affiliated company Conectiv and should therefore maintain the right to terminate and/or collect delay damages. Such a provision presents serious concerns to Bluewater investors.

Of similar consequence, Delmarva seeks a termination right in the event of a consolidation triggered by FASB Interpretation No. 46 ("FIN 46"). Bluewater has offered to incorporate terms so that it will agree to modify the PPA so as to eliminate the need for such consolidation, in lieu of a termination right. Again, such a termination would leave Bluewater and its investors with the loss of millions of dollars. Such a provision presents serious concerns to Bluewater investors.

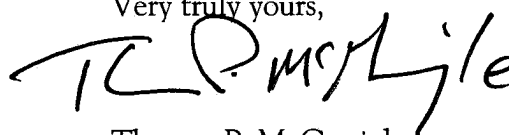
Finally, Delmarva has insisted on the right to veto any change of control of Bluewater (not to be unreasonably withheld) at any time during the 25 year term of the contract, regardless of the level of corporate ownership at which the change of control takes place. This could lead to a situation where Delmarva could block a future corporate transaction involving tens of hundreds of billions of dollars that has nothing to do with the operation of the wind farm (Delmarva has at the same time refused to accept such a restriction on itself). Bluewater believes that this is an unnecessary and unfair restriction on its ability to manage its business going forward and has proposed several compromise solutions, each of which has been rejected by Delmarva.

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In closing, with this Term Sheet, tremendous progress has been made toward making clean, stable energy a reality in Delaware. We very much look forward to a vigorous review and evaluation of the Term Sheet and stand ready to address any questions or concerns that the State Agencies may have. We also stand ready to work diligently and cooperatively with Delmarva on these remaining issues, while incorporating the already agreed upon terms into a PPA.

Thank you for your consideration of this submission.

Very truly yours,

A handwritten signature in black ink, appearing to read "TPM/Lje". The signature is stylized and fluid, with the letters "TPM" being more distinct than the following characters.

Thomas P. McGonigle

For WOLF, BLOCK, SCHORR and SOLIS-COHEN LLP

TPM/kpj